TC03671

Appeal number: MAN/2009/00042 & TC/2012/03349

VAT AND INCOME TAX – Suppression of takings and who was responsible – was assessment raised to best judgment – yes – was the quantum correct – no – alternative calculation by the tribunal – appeal allowed in part
PENALTY – Section 60 and 61 VAT Act 1994 – appeal dismissed.

FIRST-TIER TRIBUNAL
TAX CHAMBER

RAJ CUISINE (KELLS) LTD **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE JUDITH MITTING
MRS RAYNA DEAN FCA

Sitting in public at Manchester on 24, 25 June 2013, 6, 7, 8, 9, 10, January and 19 February 2014

Mr T Nawaz for the Appellant

Mr R Chapman counsel instructed by the General Council and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. Under appeal were various assessments to direct and indirect tax and associated penalties covering the period 19 January 2003 to 31 October 2007. The assessments had been the subject of amendment but as they finally fell to be determined by the tribunal were in the following form:

RAJ CUISINE (KELLS) LTD - ATHAIR KHAN											
Page	Date			Payable by co	Payable by A Khan	Revised sum		Page			
29	16-Dec-08	VAT asstt 19/1/03 to 31/10/0	66215.00	66215.00				121			
31	16-Dec-08	Pen 65%	43035.00		43035.00			125			
58	16-Dec-08	Reg 80 2002/03 tax	6254.70	6254.70							
59	16-Dec-08	Reg 80 2003/04 tax	37100.33	37100.33							
60	16-Dec-08	Reg 80 2004/05 tax	36818.29	36818.29							
61	16-Dec-08	Reg 80 2005/06 tax	35848.37	35848.37							
62	16-Dec-08	Reg 80 2006/07 tax	35627.59	35627.59							
63	16-Dec-08	Reg 80 2007/08 tax	20451.93	20451.93							
57	16-Dec-08	NICs 19/1/03 to 30/10/07	63988.18	63988.18			172101.21	236089.39			
64	12-Oct-11	Pen on PAYE/NIC 65%	153457.00	153457.00				153458.10			
45	24-Nov-08	Add'l wages 2002/03	16200.00		8185.94	1931.24			Credit given to PAYE due		
47	24-Nov-08	Add'l wages 2003/04	93600.00		37069.66	-30.67			Credit given to PAYE due		
49	24-Nov-08	Add'l wages 2004/05	94850.00		38189.30	1371.01			Credit given to PAYE due		
51	24-Nov-08	Add'l wages 2005/06	93600.00		36188.21	339.84			Credit given to PAYE due		
53	24-Nov-08	Add'l wages 2006/07	93600.00		36686.25	1058.66			Credit given to PAYE due		
55	24-Nov-08	Add'l wages 2007/08	54000.00		20347.07	-104.86			Credit given to PAYE due		
				455761.39	219701.43			176666.43			

2. All the assessments had been raised pursuant to the Commissioners' belief that Raj Cuisine (Kells) Ltd ("Kells") had been dishonestly suppressing its takings and further that its sole director Mr Athair Khan was responsible for that suppression; hence the attribution to Mr Khan of the dishonesty penalty under Section 61 VAT Act 1994. The approach to be taken by the tribunal in reaching its determination of the appeals was agreed as follows:

(i) If the tribunal was of the view that there had been suppression, that the assessments had been raised to best judgment and that the quantum of the assessments was correct, then the appeal would fail.

(ii) If the tribunal was of the view that the assessments had not been raised to best judgment, the assessments and the penalties would fall in their entirety.

(iii) If the tribunal was of the view that there had been suppression and that the assessments had been raised to best judgment but not in the correct figures, then it was open to the tribunal to carry out its own calculations on the evidence before it and to substitute its own figure for the amount of the suppression.

(iv) If the tribunal did adopt the course set out in (iii) above, then all that was required of the tribunal was to set out a methodology for arriving at its

own figure for the degree of suppression and the Commissioners would then revise the assessments accordingly.

3. On behalf of the Commissioners, we heard oral evidence from the assessing officer Mr Steven Hancox and from the following officers who had carried out observations:

Paul Younger

Judith Bleasdale

Karen Wilkinson

Christopher Tait

A number of other officers had also been concerned in the observations and witness statements from all of them were before the tribunal. Mr Nawaz, in order to save the time of the tribunal, stated that he would not be asking the remainder of the officers to give evidence as, although their evidence would remain challenged, he would merely be asking them the same questions which he had already asked the four above named officers.

4. On behalf of Kells, Mr Athair Khan gave evidence.

Background

5. Kells, operating as a licensed restaurant and takeaway, registered for VAT with effect from 19 January 2003 and deregistered from 31 October 2007. Throughout Mr Khan was its sole director. Mr Khan had previously been the sole director of Raj Tandoori Restaurant Ltd ("Tandoori") which had commenced trading on 7th June 1998, date of cessation not known. Both restaurants traded as "The Last Days of the Raj". From 26 November 1985 to 1st July 1993, Mr Khan also traded in partnership with others as The Last Days of the Raj, this business being acquired by Mr Khan's wife, Mrs Nepur Nessa Khan, who operated it from 28 September 1994 to 14 April 1997.

The Special Compliance Office investigation

6. Tandoori, the partnership and Mrs Khan had all been the subject of a direct tax Special Compliance Office ("SCO") investigation covering the period 1 February 1986 to 30 June 2000. A Disclosure Report, prepared by Mr Khan's advisors, was signed off by Mr Khan on 13 August 2001 and the Settlement Report was signed off by HMRC on 1 March 2002. We go into greater detail about the investigation later in this decision as the findings were to form a central part of both parties' cases and the conduct of the enquiry was central to Mr Khan's case. We will however at this stage set out some basic information which emerges from the reports. It should be noted that of the two reports, Mr Hancox had not seen the Disclosure Report when he raised his assessment, this not being seen by him until immediately before the tribunal

hearing. Mr Hancox had seen, and relied upon the contents of, the Settlement Report but Mr Khan had not seen this report until 15 January 2014.

7. It is apparent from the Settlement Report that Mr Khan had had three sets of advisors. The accountant for the investigation was a Mr M D Hossain. Mr Hossain was not an expert in SCO enquiries and Mr Khan's specialist accountant was named as Mr P Ford.

8. The Settlement Report refers to three test meal visits undertaken on 10 October 1998, 4 December 1998 and 4 March 1999. Suppression of meal bills was found on all three visits. The section relation to Opening and Disclosure details contains the following two paragraphs.

> "Khan's initial disclosure following the replies to the Hansard Questions were that tips had not been fully recorded, that the cash tips had been taken for himself and there was nothing else wrong with the accounts or Returns. He estimated this between £200 and £280 per week.
>
> After almost a 7 hour meeting, which included 6 breaks for further reflection, Khan changed his mind several times, and his final disclosure by the end of the meeting was totally different. By the end of the meeting, he had disclosed omitted cash sales of £600 per week taken for himself, together with a further £400 per week unrecorded cash sales to pay staff wages. In addition, tips of £500 per week were taken, of which £250 was for himself, and the remaining £250 was to pay top-up wages. Additional PAYE was due on all additional staff wages."

9. There is further reference in the Settlement Report to an £18,000 legacy which Mr Khan was said to have received from his late father but which the advisors treated as additional sales as "the agent realised that this explanation would not be acceptable to the Revenue without evidence …". This addition is later referred to by the officers as an "arbitrary" addition to sales.

10. The final settlement for all three businesses was agreed at £119,119.52. The weekly suppression figure for the final year of the enquiry (year ended 30 June 2000) stood at £1,650. £650 was said to have been used to pay off record wages and the remaining £1,000 per week being taken out by Mr Khan. It was this figure of £1,650 per week that Mr Hancox picked up and was to take forward into his consideration of the assessment.

11. The SCO report lists the assets of Mr and Mrs Khan and their children. It calculates amounts of undeclared profits in the businesses. It does not include any reconciliation between omitted profits and assets.

The enquiry the subject of this appeal

12. This enquiry began when the Commissioners received an anonymous phone call on 10 February 2004. A contemporaneous note was made of the call. The existence of this call was not disclosed to Mr Khan until a meeting which took place on 14

January 2009 attended by a Mr J Kellett, newly appointed advisor to Mr Khan, and Mr Hancox. In readiness for the meeting, Mr Hancox had prepared for Mr Kellett a briefing note outlining the course of the investigation to date. The first paragraph of the note read as follows:

> "Anonymous call received early in 2004. Caller stated that the restaurant normally takes between £10,000 and £13,000 per week but only declares about half of this and destroys 'bills' regularly by burning them. The caller also stated that Khan was paying his staff (stated as 10 full time waiters and 5 or 6 full time chefs) more than double the amount he is declaring. He was said to be showing around £120 per week in the books and actually paying around £300 per week."

On the first day of the tribunal hearing, Mr Nawaz sought disclosure of the contemporaneous note itself. We read the note and refused Mr Nawaz's application. The final sentence of the note could well have identified the identity of the caller and in any event took the matter no further. We were able to assure Mr Nawaz that the summary of the call contained in the above paragraph was accurate.

13. In response to the tip off, the Commissioners began their enquiry by arranging a test eat and observation programme. This took place on Friday 26 November 2004 and Thursday 9 December 2004 and took the following form:

Friday 26 November 2004	Time	Observers
Lunch	12.35 - 14.00	John Mitchell and Jean Wright
Dinner	18.20 - 20.10	Elspeth Graham and Clive Graham
	19.45 - 21.30	Pat Robertson and Bill Robertson
	20.45 - 22.20	Paul Younger and Marie Milne
	21.50 - 23.30	Alison Field, Stuart Thompson and Kevin Brooke
Take Away	18.55	Lynn Burlace
Take Away	20.55	Bill Emerson
Thursday 9 December 2004		
Lunch	1210 - 13.30	Kirsty Bambrough and Marion Hannigan
	13.12 - 14.30	Eve Watson and Nicky Dorricot
Dinner	18.15 - 19.35	Sharon Howe and Deborah Johnson
	19.00 - 20.55	Judith Bleasdale and Craig Bleasdale
	20.25 - 22.25	David Brown, Clare Brown, Denise Horsley and Chris Tait
	22.05 - 23.55	Andrew Gibson and Karen Wilkinson
Take Away	19.55	Billy Emerson
	21.00	Paul Younger

14. Mr Bill Robertson had conducted what was called a "scoping" visit on 29 October 2004. He had produced a set of notes including directions, parking facilities, advertising literature and a plan. The plan had been drawn from memory and, not surprisingly, contained a number of inaccuracies. The partitioning (trellis) was not marked; pillars were in the wrong place and the tables were not entirely accurately placed. The plan does not appear to have been given to all the observing officers. Mr Younger could not recall whether he had seen it whereas Mrs Bleasdale and Mrs Wilkinson were adamant that they had not. Mr Tait had seen it and remembered having seen it. It appears that none of the officers used it for the purpose of marking where they had sat and where they had observed other diners. This omission was much criticised by Mr Nawaz.

15. It should be borne in mind that the four officers who gave evidence to the tribunal were giving it some 10 years on. They had made witness statements in 2011 but even that was some six years after their visit. It is therefore hardly surprising that the evidence that they gave was not entirely satisfactory and was contradictory in part. Examples include that Mr Younger had no recollection of a partition formed of planters and trelliswork whereas Mrs Bleasdale and Mrs Wilkinson both recalled it. Mrs Bleasdale was certain that she had seen an electronic till which she could not have done. Mr Younger could not recall the procedure which should be adopted when they arrived. He could not remember whether he would have counted the officers he took over from. He could only say that whatever he did would have been in accordance with instructions. Despite the presence of the trelliswork which could have obscured visibility from certain areas of the restaurant, all four officers were certain that they had a sufficiently good view to observe comings and goings and that their notes accurately recorded what they had seen. They spoke of making eye contact with the group they were taking over from or who were taking over from them. Mr Younger said that they "kept moving around". They all referred to making notes on their mobile phones. There was further confusion as to whether or not Mr Khan had been on the premises. Neither Mr Younger nor Mrs Bleasdale could recognise him as having been in the restaurant but Mrs Wilkinson was certain that she had seen him. However the description which she gave in her witness statement of "a stout middle aged man wearing spectacles … casually dressed, wearing a track suit top" was accepted by the Commissioners not to have been Mr Khan. Mr Tait was quite certain that he had seen Mr Khan. He described having looked up the restaurant on the internet and seeing pictures of Mr Khan. Mr Tait had also seen pictures of Mr Khan on advertisements on local buses and he recognised him as the person he saw on the premises during his surveillance.

16. The observations had been set up by a Mr Conlon who did not give evidence but we were referred to a summary document which he had compiled from the notes of all the observing officers. This document lists the dates and times of the observations; the tables at which the officers had sat; the meals they had ordered and their cost; the staffing and importantly the number of diners and groups which they had each observed. At the foot of his summary he had added the following:

> "Further information, unreliable as may be double counting: one group of three and one group of eight."

This note refers to the fact that on 9 December, the group which entered at 20.25 observed one group of three and one group of eight. The following group who arrived at 22.05 also noted that they observed one group of three and one group of eight. It was quite clear that these groups had been double counted. This note of Mr Conlon's was put with the case papers and would have been transferred with the papers to Mr Tait who took over the course of the enquiry and then on to Mr Hancox when his enquiry opened. We make further reference to this matter when we speak later of Mr Hancox's calculation of the suppression.

17. On 26 November 2004 a total of seventeen parties had been recorded as dining at the restaurant of which five were HMRC parties. A later review of the business records for that day would reveal that there were only eleven restaurant bills amongst the records. All of the HMRC meals had been paid for in cash and none of these bills were amongst the records. One other customer's bill was also omitted. On the same day two HMRC staff had purchased take away meals, again paying in cash, and neither of these bills were included in the business records either. The omitted HMRC restaurant bills totalled £228.05, including tips of £11.70.

18. A similar calculation for 9 December revealed that just two of the HMRC bills were declared (including one paid by credit card). Those not declared totalled £234.35 including tips of £10. There were additionally found to be four unrecorded non-HMRC bills. Additionally a further two HMRC cash take away bills had also not been declared.

19. In summary therefore for the two days of observation, none of the HMRC takeaway bills had been declared. On 26 November none of the HMRC dining bills had been declared and there was also one non-HMRC bill not declared. On 9 December there were just two HMRC bills declared (including one credit card payment) and four non-HMRC bills undeclared.

20. Having carried out the observations, the Commissioners then waited until they received the company's tax return for the period ended 31 January 2005. At that stage Mr Tait, who by that time had taken over conduct of the case from Mr Conlon, was in a position to open his enquiry. This he did on 7 November 2006 when he wrote to Messrs Hossain Moorehead and Co, accountants to the company, advising that he was enquiring into the company's return for the year ended 31 January 2005 and asking for a full set of the books and records from which the accounts had been prepared. A great deal of further information and analysis was also requested. By letter dated 27 November 2006, the records were submitted to Mr Tait and were acknowledged on the 6 December. Reference was to be made in a later note to some confusion over whether or not the purchase invoices had been submitted. Having heard Mr Tait's evidence, we are satisfied that the letter of 27 November did contain a full set of purchase invoices. Once Mr Tait had received and had examined the records, with specific reference to the recorded meal bills for the observation days, he formed the view that there had been not only suppression but a suppression of such a scale that the enquiry should be escalated into one of fraud and he passed his file on to Mr Hancox to open a CIF investigation. This would appear to have been in March 2007.

A meeting was requested by letter dated 11 May 2007 but it was not until mid October that Mr Khan was able to attend any such meeting.

21. A long and wide reaching meeting took place on 17 October 2007 attended by Mr Khan, accompanied by Mr Hossain and Mr Ford, his advisors, and Mr Hancox and Mr Vickers of the CIF team. We were referred to the notes of that meeting prepared by Mr Vickers and later to be sent out to Mr Khan for approval. In response to the four VAT related questions, Mr Khan replied that no transactions had been omitted; all books and records were correct and complete; all returns were correct and complete and he was unaware that any VAT returns were incorrect or incomplete at the time of submission. That declaration is dated 17 October. In relation to the five direct tax questions, Mr Khan answered verbally that no transactions had been omitted or incorrectly recorded; the accounts lodged with HMRC were correct and complete; all tax returns had been correct and complete, all personal tax returns had been correct and complete and that he would allow an examination of all records business and private.

22. The notes go on to show a wide range of topics were discussed. Mr Khan described how Kells operated – trading hours, suppliers, ordering procedures, cashing up procedures, business records, his own drawings and emoluments, staffing and the payment of wages. At paragraph 35 of the notes the following is recorded:

> "He explained that he might start work two hours after the restaurant opened and was not present at cashing up time every day. He relied on his staff to cash up sometimes three times per week. MJV asked if some staff members had worked in the restaurant for a long time. AK said that staff would come and go. Full-time staff tended to work for six to seven months before leaving. The longest serving member of staff was said to have worked for three years. MJV asked AK for the names of his trusted staff. AK mentioned Mr Rahman, Mr Raja and Mr Sabeer. The first two gentlemen are no longer working in the restaurant."

There followed extensive discussion of Mr Khan's personal history, lifestyle his own personal assets and liabilities and those of his family.

23. The meeting concluded with the following recorded at paragraph 66:

> "MJV then advised AK that during the 2005 accounting period more than one visit was made to the restaurant. Test purchases were paid for in cash for both restaurant and take away meals and these purchases were not found amongst the business records."

24. The notes of the meeting were sent to Mr Hossain on 6 November for signature or amendment. By letter dated 15 November a set of amendments and corrections were returned. Of specific relevance was the following:

> "Section 66

MJV states in section 66 that the test purchases of both restaurant and takeaway meals had not been found in the business records. Thus it can be gathered that there are some missing bills in question. Therefore it is a case of bills being missing, I am concerned that the information I provided at the meeting relating to an incident of staff steeling (sic) bills are vital facts which have not been included in the notes. This would seem to be essential information which may help to justify or be 'capable to provide explanation' in order to resolve the matter.

MJV has not recorded in the notes that I mentioned of an incident in the past regarding a missing bill. Many staff members were suspicious over the odd behaviour of a particular employee. This concern was drawn to my attention and I retained an observant eye on the activities of the employee, namely Mr Shafiqur Rahman. Mr Rahman was in charge of the restaurant floor at times when I was not present and he carried out duties of cashing up. His employment was terminated when he was caught with theft and he no longer works at the restaurant."

The response to the corrections came in a letter from Mr Vickers to Mr Hossain dated 5 December containing the following two paragraphs:

"Section 66

Both I and my colleague recall Mr Khan referring to the possibility of staff theft. Neither of us recall any reference being made to many staff members being suspicious over the odd behaviour of one particular employee. Likewise, we have no recollection of Mr Khan naming this employee as Shafiqur Rahman or reference being made to Mr Rahman's employment being terminated. Your client had of course previously named Mr Rahman as one of his trusted employees. Had I been made aware of the fact that his employment had been terminated, I would have certainly wished to have asked some questions regarding the grounds Mr Khan had for doing this.

Third party interviews

I hold information which leads me to believe that the company's sales may have been understated. Mr Khan has stated that he is not responsible for any such understatement and has suggested that it may be the result of staff theft. In view of the amounts potentially involved it is clearly necessary to test this as best one can. The best way of doing this would seem to be to carry out interviews with a number of former employees."

25. As indicated in the letter of 5 December, Mr Vickers and Mr Hancox interviewed three former employees of Kells. The notes of these interviews had not been disclosed to Mr Khan but were before the tribunal. On application by Mr Nawaz for disclosure, we released them to Mr Nawaz personally in redacted form on condition that they were not shown to his client. On reading the notes, Mr Nawaz made a further application that he be allowed to disclose them to Mr Khan in order that he

could take instructions. This application was refused on Mr Chapman's undertaking that the Commissioners had not relied upon the notes in any way and they would form no part of their case. Employee number 1, who had been a chef, had been asked what duties Mr Khan would undertake when working and replied that he would "sometimes be behind the till or front of house, sometimes in the kitchen and sometimes he would simply talk to customers". He described Mr Khan as always being present in the restaurant. He was asked if he had ever been aware of any cash going missing from the till and said he could recall this happening on three occasions. Mr Khan had sat the staff down and asked who had taken his money. He recalled one employee being dismissed for theft in 2002 or 2003 but could not recall the name. Employee number 2 again said that Mr Khan was normally present at the restaurant. He had not been aware of any cash missing from the till or any front of house meal bills being destroyed. He was not aware of anyone being dismissed for theft whilst he worked there. He was specifically asked if he had been aware of any top up wages being paid and he was not. Employee number 3 said that Mr Khan was rarely at the restaurant and when he was he would come and go. He said that he had worked at the restaurant in 2005 for approximately one year and during that time "Mr Khan did not seem particularly interested in the restaurant". This employee also said that he was not aware of any meal bills being destroyed and he was not aware of anyone being dismissed for theft.

26. Mr Hancox and Mr Vickers had also interviewed and corresponded with two of Kells' main suppliers. It is not necessary to go into any detail on this aspect, suffice it to say that Mr Hancox accepted that there was no record of any discrepancy between the restaurant and suppliers' records.

27. Over the following months (beginning of 2008), the Commissioners proceeded to carry out exhaustive and extensive enquiry into the means of Mr Khan and his family. They looked at assets, properties, investments, loans, bank accounts and living expenses. As far as we can see from the correspondence, and indeed this was not contradicted by Mr Hancox, Mr Khan, through Mr Hossain, co-operated fully, providing all documentation and information that was requested.

28. A further meeting took place on 17 June 2008 at which Mr Hossain was present (but not Mr Khan) with Mr Vickers and Mr Hancox. At this meeting Mr Hancox did provide limited information with regard to the test purchases. Mr Hossain was told that two visits had been undertaken during the year ended 31 January 2005. Mr Hancox advised Mr Hossain that on the first occasion there had been five HMRC parties who paid in cash, none of those bills being amongst the records plus one further customer's bill also omitted. Mr Hossain was told that the sums spent by HMRC staff totalled £228.05 – none of which was reflected in the business records. On the second occasion, Mr Hossain was told that a total of 24 parties (Mr Hancox had still not picked up Mr Conlon's rider re duplication of observation) dined in the restaurant of which six were HMRC staff. It was found, Mr Hancox said, that four HMRC bills were omitted from the records plus those for seven other customer groups. Mr Hancox advised Mr Hossain that the total HMRC spend omitted on that second occasion was £234.35. Mr Hancox added that if the two evening's concealed HMRC purchases were averaged it would come to £231.20 per night or £1,618.40 per

week. This, pointed out Mr Hancox, was very close to the admitted SCO level of extraction. The remainder of this meeting appears to have covered no more than, again, extensive discussion of assets and capital.

29. By letter dated 2 September 2008, Mr Hossain replied to Mr Vickers confirming that Mr Khan's answers to the five direct tax and four indirect tax questions remained the same. He also asked for further information regarding the two observation visits. He asked for dates, the size of each party, what was purchased, how was payment made, copies of the bills and a deal of further surrounding information. He also in this letter added extensive further information regarding Mr Khan's income and life style expenses. He advised that Mr Khan's weekly wages from the business were £350 plus a further dividend payment of £250 which went straight from the Kells account into his personal account. Additional cash would be taken if needed. All cash wages had been fully recorded. He and his family lived cheaply. They ate cheaply and shopped cheaply. He only ran a P registered Nissan Micra and had no expensive hobbies or pastimes. He did not smoke or drink.

30. Mr Hancox replied to Mr Hossain by letter dated 7 October advising him

> "You have requested information and documents in relation to the two visits HMRC staff made to The Last Days of the Raj. The appropriate information and documents will be provided in due course as part of the appeals procedure"

Mr Hancox was pressed in cross-examination as to why he had refused to disclose further information of the observations. His answer was that he had attended a number of case conferences internally and it had been decided to proceed as they did and that was the advice which he had been given.

31. By the end of October 2008, Mr Hancox decided that he had sufficient information to raise the assessments. He duly wrote to Mr Khan on 30 October advising him accordingly. To calculate the assessments Mr Hancox clearly had to establish first the degree of suppression. He adopted what Mr Chapman was later to call the "broad brush" approach and we can do no better than to take the wording of his witness statement to describe his process.

> "When estimating the likely understated takings I took into account the following factors:
>
> - the level of HMRC purchases that had been omitted from the business records i.e. £216.35 on 26 November 2004 and £224.35 on 9 December 2004
>
> - That a significant amount of cash received from other customers was likely to have been extracted (for example, on 9 December 2004, the second visit, a total of 18 non-HMRC parties were seen dining in the restaurant but only 11 bills (61%) were found in the records), and

- that the HMRC test purchases would have increased the level of cash takings on those days (as had already been stated in the Appellant's letter dated 2 September 2008).

I concluded that it was likely that takings averaging £1,800 per week or £93,600 per annum had been omitted from the business records. The omitted HMRC purchases averaged £220.35 per night which equates to £1,542.45 per week. Omitted takings from other customers also needed to be taken into account. I considered it unlikely that the off record takings would have been less than they were during the period covered by the SCO enquiry and concluded that a sum of £1,800 per week was realistic. I thought it was likely that the level of omissions had been approximately the same since the company commenced trading."

32. Mr Hancox raised the direct tax assessments on 24 November 2008 and the indirect tax assessment on 16 December 2008 together with the notification of civil penalty.

33. Mr Hancox was pressed in cross-examination by Mr Nawaz as to his justification for extending the assessment back to the commencement of trading. It was put to Mr Hancox that Raj Tandoori had ceased trading almost immediately after the SCO enquiry and from then until January 2003, the business had been run by a Mr Ali with Mr Khan only being employed and there was therefore no continuity. Mr Nawaz asked if Mr Hancox had any evidence of wrong doing between the SCO settlement at the end of 2001 and the observations in 2004. Mr Hancox said that he had not but that in his mind Mr Khan's involvement in the business never ceased. He went from being a director to an employee back to director all in the same business, even though a different legal entity.

34. It will be noted from the extract above that Mr Hancox had calculated that only 61% of the restaurant bills for 9 December 2004 were found in the records. This figure was reached because Mr Hancox had not factored in Mr Conlon's comment on the duplication. At the beginning of his evidence, Mr Hancox sought to correct his calculation to reflect the duplication and the correct figure should be that 68.75% of bills were found in the records as opposed to 61%.

35. In his evidence in chief, Mr Hancox said that he had carried out an alternative calculation of the suppression based on the seemingly omitted bills for other customers. On his original figures, this would have produced a weekly suppression of £2,435 which he thought unlikely. The same calculation based on the revised HMRC party numbers produced a suppression rate of £1,826 per week which he thought would be more realistic.

36. Mr Hossain wrote again to the Commissioners by letter dated 12 December 2008 asking again for the details of the observations. In response Mr Hossain was told "all documentation that HMRC will rely upon during the appeal hearing will be provided during the mutual exchange of documents procedure". He reiterated in the same letter that Mr Khan had throughout denied any personal wrongdoing but put the blame on members of his workforce. Mr Hancox found it difficult to believe that his staff could

have been extracting such large amounts of cash from the business without Mr Khan's knowledge, especially bearing in mind that Mr Khan had previously admitted to significant understatements. The dates of the visits were eventually provided to Mr Hossain by letter dated 5 February 2009. Mr J Kellett of Kellett Tax Consultancy Limited then became involved and by letter 17 February 2009 sought the rest of the information that Mr Hossain had requested in September. In response, by letter dated 27 February 2009 Mr Hancox provided a schedule of the HMRC purchases.

37. A meeting took place on 14 January 2009 between Mr Hancox and Mr Kellett. In readiness for the meeting, as we have referred to above, Mr Hancox prepared a briefing note for Mr Kellett. This is an interesting note because, as Mr Nawaz pointed out, it was written within days of the raising of the assessments and is therefore a strong reflection of the matters central to Mr Hancox's thinking when the assessments were raised. We have already noted the reference to the anonymous phone call in the briefing note. Other points referred to in the notes include the following. Mr Khan was seen working on the premises on the second observation night. The records revealed an unusually high credit card percentage of 69.11%. There were contradictory notes with regard to purchases from the two main suppliers, one entry stating no purchase invoices had been received and the other that purchases had been checked and were in order. The note also refers to a Chi Squared test which was carried out on the recorded cash tips for the year ended 31 January 2005. This was shown as revealing only a one in nine chance of the recorded tips being correctly recorded. The note goes on to refer to Mr Rahman and reveals a misconception under which Mr Hancox was labouring. The note refers to Mr Khan's statement in the meeting of 17 October that he had had three trusted members of staff including Mr Rahman. Mr Khan then, the note goes on, had referred to "the trusted employee Mr Shafiqur Rahman being dismissed for theft". In fact, Mr Khan employed five members of staff by the name of Rahman. One was his trusted employee and another was Shafiqur who was the suspected thief. The note also contains reference to Mr Rahman having ceased employment on 19 February 2005 and notes that former employees being interviewed had no knowledge of an employee being dismissed for theft at that time. The final paragraph of the note simply questions whether or not Mr Khan had continued to carry on what he had admitted to previously.

38. Mr Nawaz was then to become involved on behalf of Mr Khan to conduct the appeal and further correspondence and meetings took place between Mr Hancox and Mr Nawaz.

39. In addition to Mr Hancox's original and main witness statement, by the end of the hearing we had three further witness statements from Mr Hancox, the first two being put in prior to the hearing and the third in circumstances we describe below, during the hearing.

40. The second witness statement sets out in greater detail the raising of the assessments. The third witness statement answers challenges made by Mr Nawaz as to why a capital statement had not been prepared. Mr Hancox states that full capital statements require a detailed accumulation of information about capital worth, income and expenditure. The accuracy of such a statement is dependent upon the accuracy of

the information provided. As Mr Khan was continuing to deny any personal benefit from the irregularities, Mr Hancox's view was that he would not admit to the true level of his personal and private expenditure or assets and without this the preparation of capital statements was pointless.

41. The fourth witness statement of Mr Hancox concerned a matter which arose during the course of his evidence. In answer to questions from the tribunal, Mr Hancox stated that he had believed that Mr Khan was taking money out of the business to fund his lifestyle. He added that he had had a suspicion that there may be assets held in the name of others that were in reality Mr Khan's. This had not been raised before either in correspondence, in his original witness statement or in the course of his evidence. Mr Chapman took this point up in re-examination when Mr Hancox admitted that when he raised the assessment he had had "hard evidence" of the purchase of a property in a name other than Mr Khan. This was, he accepted, a factor which he took into account when considering the assessments. In his fourth witness statement and further oral evidence, Mr Hancox explained that the property over which he had concerns was number 45-46 West Sunniside, Sunderland. This property had been purchased in December 2002 by Miss Halema Khan, the daughter of Mr and Mrs Khan. She had sold it in February 2004. During the period of her ownership she rented it out and made mortgage repayments. Mr Hancox had no concerns over the funding of the property or the proper tax treatment of the rent and mortgage repayments. However he had become aware that out of the sale proceeds, Miss Khan had loaned her mother £70,000 to fund the extension on Mr and Mrs Khan's property. Mr Hancox outlined two scenarios. One was that Miss Khan had identified a property she would like to buy, did so and rented it out, sold it and out of the sale proceeds offered a loan to her mother to pay for an extension. There was nothing wrong with this scenario. However an alternative scenario was that Mr Khan had identified a property he would like to purchase and arranged for it to be purchased in his daughter's name. It was then rented out prior to sale. On sale the capital gains tax payable would be lower than it otherwise would have been because the property was registered in his daughter's name and the profit made on the disposal would be used by Mr Khan, as had always been his intention.

42. On further questioning by Mr Nawaz, Mr Hancox accepted that he was not saying that funds had been extracted from Kells to use in the purchase. He accepted that he could not show that the acquisition of the property had been funded by Mr Khan or had had any impact on the tax liabilities of Mr Khan. He confirmed that the property had no impact on the assets of Kells. He accepted that the £70,000 loan to her parents had no tax repercussions to Kells and that the funding of the property had no direct or indirect impact on the company's liabilities. His concern was that Mr Khan had seemingly benefited from the sale of an asset held in another's name. Mr Hancox went on to say that he thought it unlikely that the loan would be repaid but he had no information as to whether or not it was being. He also thought it likely there would be other examples which he had not discovered.

43. Mr Hancox further accepted that he was not aware of Mr Khan having an interest in any properties other than those which had been disclosed. Equally he was not aware of any other bank accounts, deposits or assets other than those disclosed. He

did however remain suspicious throughout that Mr Khan was dissipating his assets and that he was purchasing properties in the names of others of which he remained beneficial owner. He accepted that of the properties and assets of which he was aware he was satisfied with their funding and that there had been sufficient funds available outside the business to acquire the properties and to fund related loans. In answer to a question about the impact of the additional sales which the assessments would attribute to the company, Mr Hancox replied that if he added the additional sales on to the returned sales, a gross profit rate of 74% for the year in question would be reached. This, said Mr Hancox, was within HMRC guidance of 60 to 69% as the guidance goes on to say that fluctuations can be wide. Mr Hancox referred to the business as being an "up market restaurant which had won awards and attracted up market customers and celebrities". He could not name any but was aware of a rather unsavoury incident when a very drunk ex footballer visited the premises and caused a lot of damage. The police had been called and the incident did attract media attention. When questioned further about the SCO enquiry, Mr Hancox commented that Mr Khan would be in need of money to repay the settlement figure. A loan had been taken out to make the repayment and Mr Hancox was aware that this loan was being repaid directly out of an account in Mrs Khan's name, this account being fed by rental income on properties owned by her. He accepted that he could find no evidence of extractions from the current business to meet the settlement repayments.

44. Mr Hancox also accepted, in relation to the tip off call, that there was no evidence of the burning of bills and no evidence that more than double the declared amount of wages was being paid out. There was no evidence of off-record wages or top up wages. Equally there was no evidence of suppression at the rate implied by the note.

45. Mr Hancox was asked to explain the chi squared calculation. We were told it was a mathematical formula which looked at a set of figures and purported to establish whether or not the figures were realistic for example whether a number 9 appeared more often than it should. Applied to the schedule of recorded cash tips, the test had shown that there was only a one in nine chance of their being correctly recorded.

46. The jist of Mr Hancox's evidence was that he had clear and irrefutable evidence of suppression on the two observation nights. He had clear evidence from the Settlement Report that Mr Khan had previously admitted to large-scale suppression. He did not accept that the explanation for the current suppression was down to thieving by employees and this only left him with Mr Khan. His calculations from the observation nights brought a figure not far below that of the earlier suppression and he saw no reason why the current level should be any less than previously.

Evidence submitted by an on behalf of the Appellants

47. We deal first in this section with the evidence given by Mr Khan. We have taken this evidence from his written witness statement and from his oral evidence

48. Mr Khan's business activities began in November 1985 when, in partnership with others, he began trading as The Last Days of the Raj. There followed Tandoori, Raj

Cuisine Ltd (of which Mr Khan was an employee) and Kells which commenced trading on 19 January 2003 and ceased on 31 October 2007.

49. Mr Khan has a history of continuing ill health, having suffered severe injuries in a criminal attack on him on 9 December 1991 and further serious injuries in a road traffic accident in 1999. It is clear from medical evidence which we have seen that certain of the injuries were neurological and we were told that he has continuing serious problems with his memory.

50. Mr Khan's evidence in chief began with a description of the SCO enquiry. His then accountants had had no experience of such enquiries and recommended him to Mr Hossain who, in turn, had approached two well known firms both of which had quoted fees in the region of £40-60,000 which Mr Khan could not afford. Mr Philip Ford had then been instructed. He was not so expensive but, as submitted by Mr Nawaz, was not so experienced either. We were referred to the Settlement Report, Paragraph 5.2 of which is headed "Standard of Accountant's work during the case". Mr Ford is described as being thorough in his preparation of the report having relied heavily upon the disclosure made at the Hansard Meeting. It was pointed out that he had used Mr Hossain to help him in the preparation of the report but that, in this particular context, Mr Hossain's work was "not to be relied upon" due to his inexperience in such enquires. We should make it clear that there was no criticism whatsoever of Mr Hossain's integrity or competence in the other types of work with which he was better acquainted.

51. The initial SCO meeting had taken place on 26 Aril 2000. It was attended by Mr Khan, Mr Hossain and Mr Ford and, on behalf of the Commissioners, by a Mr Campbell and a Dr Cox. The Settlement Report contains the following description of the meeting

> "After almost a seven hour meeting, which included six breaks for further reflection, Khan changed his mind several times, and his final disclosure by the end of the meeting was totally different."

The Settlement Report refers to Mr Khan replying to the Hansard questions to the effect that transactions, receipts and expenses had been omitted from or incorrectly recorded in the business books; that his accounts and taxation returns were not correct and complete; that his personal returns were not correct and complete but he was prepared to allow full access and co-operation.

52. As Mr Khan gave his evidence, he became upset and emotional as he recalled the meeting and a break was given for him to compose himself. He told us that when the Hansard questions had been put to him initially he had forcefully denied any wrongdoing. He had maintained repeatedly that his records had been correct and that his returns were correct and that there were no omissions. At this point Mr Campbell, who was described as large and loud voiced, started shouting at him. Mr Campbell threatened him with imprisonment if he continued to refuse to acknowledge his wrongdoing. Mr Campbell's manner was described as menacing, bullying, intimidating and, we were told, he repeatedly instructed Mr Ford to take Mr Khan out

and "come back with the answers". Mr Ford did repeatedly take Mr Khan out into the corridor and is said to have reiterated that he could be imprisoned if he did not make admissions and he advised Mr Khan initially to make a small admission such as unrecorded tips. The meeting went on with Mr Campbell repeatedly refusing to accept that there were only small omissions and Mr Ford repeatedly advising Mr Khan to admit to more and more and greater and greater amounts. It was, said Mr Khan, like torturing him as Mr Campbell became more and more angry and threatening to handcuff him and put him straight into a cell. There is some slight discrepancy here as Mr Khan described to us that it was so dreadful that his wife was crying whereas in the Settlement Report it is stated that Mrs Khan did not attend the meeting, although she had been invited. Eventually, Mr Khan told us, he had been so terrified that he had made the admission of substantial suppression. In his evidence to us however he repeatedly denied any wrongdoing and maintained that the admission he had made was utterly false, but something which he was forced into both by Mr Campbell and indeed by his own advisors. He had made the admission, albeit totally false, "to get back his life".

53. Mr Khan, as we have said earlier, did not have sight of the Settlement Report until the tribunal hearing. It is the Settlement Report which contains the details of the observations which were to form the basis of the SCO enquiry. Mr Khan told us that the reference to the observations contained in the Settlement Report was the first he knew of there ever having been any observations and this was something that was never put to him during the seven hour meeting. He said that he never knew what the enquiry was about. He was referred by Mr Nawaz to the section of the Settlement Report which referred to the £18,000 legacy left to him by his father but which Mr Ford said had to be treated as undeclared sales. Mr Khan stated that he had no recollection of this.

54. Mr Khan signed off the Disclosure Report at a meeting at Mr Ford's office on 13 August 2001. Mr Campbell and Dr Cox again both attended the meeting at which Mr Campbell again, we were told, warned Mr Khan that if he committed any further acts of suppression he would be imprisoned without trial. He was told that an inspector would be watching him the whole time. The settlement sum was paid by Mrs Khan who re-mortgaged her properties. In return Mr Khan gave up his interest in the matrimonial home. We were told that from 2001 until 2007 when he received the first letter regarding the current enquiry, he had had no problems or difficulties with HMRC.

55. Turning to the current enquiry, a great deal of Mr Khan's evidence, both oral and written, concerned the observations. He was quite certain that he would not have been present in the restaurant on either of the two observation days. Over that period he was having an extension built to his home which had started in October 2004 and continued to well into the New Year. It was not going according to plan, requiring him to be on site for a large part of the time. Additionally his daughter was getting married in January 2005 and his time was much taken up with preparations for the wedding.

56. Although he had received notice of the observation dates far too late for him to be certain of his movements, he had checked the meal bills for the days to see if they were in his writing. His role in the restaurant was to greet customers as they came in, take them to their tables, take their orders and generally wander round talking to them and being "the host". All meal orders would therefore be in his handwriting if he had been on the premises. The only bill to have his writing on, he told us, was a bill, to which we were referred, for 9 December 2004. It is for a party of nine at twelve noon. There is a reference at the top of the bill to it having been a prior booking and the main orders, we were told, were all in Mr Khan's writing. There were however two entries on the bill, one for drinks and one for ice cream which were not written by him. The explanation would have been that he would have taken the original order prior to the 9 December possibly over the phone or one of the party may have called in to place the order, but the additional entries would have been taken by the waiters on the day and as they were not in his writing he cannot have been there.

57. Additionally, it was his invariable practice to wear a dark suit of which he had two. One had the words "Athair Khan" embroidered in gold on the lapel and another had a badge on the pocket with an elephant logo and "The Last Days of the Raj" written on it. If one suit was being cleaned he would wear the other one. The staff wore dark suits or plain jackets and because of such variations he was in no doubt that had any of the officers seen him they would have referred not to a dark suit but to the embroidery or the badge. As none did it follows that he was not there. Additionally Mr Khan had never owned or worn a tracksuit. It followed that the officer who had identified the owner by the fact that he was wearing a tracksuit was mistaken. The only person that Mr Khan could recall having worn a tracksuit top was Shafiqur Rahman.

58. Mr Khan then referred to the observations themselves. He was highly critical of the scoping plan and produced his own plan and a number of photographs. He pointed out the absence in the scoping plan of the partitioning wall of planters. Where the plan describes six tables for two, there were in fact five tables for four. The presence of the partitioning trellis was especially important because certain of the officers, if they were sitting where they indicated, would have had an obscured view.

59. It was also, said Mr Khan, not the case that everybody who came into the restaurant came to have a meal. Suppliers, friends or relatives or people seeking employment could all come in. In particular potential customers who were coming in to discuss a future booking would be taken to a table and served with a complementary cup of coffee and/or a starter or could be given a sample of any dish they asked for. He took us to the takings for 9 December which showed one previously booked party had paid a deposit of £45 and those for 10 December show four parties with deposits having been paid earlier. There was a slight discrepancy in Mr Khan's evidence here. In his witness statement he merely referred to the fact that people who had made party bookings would pay their deposits "earlier". In his oral evidence he referred to them as coming in at the latest 24 hours before.

60. Mr Khan attributed the suppressed takings on the two observation evenings to a former employee Mr Shafiqur Rahman. Mr Rahman was in England on a one-year

work permit and we were shown his employment record which revealed that he had started work in April 2004 alongside another permit holder. It would have been expected that he would remain in post until April 2005 as did the co-worker, but in fact Mr Rahman's employment had been terminated in the February. The reason for this was that he had been sacked for stealing. Mr Khan said that in approximately November 2004 he had heard whisperings that Mr Rahman was stealing but he had been so pre-occupied with the extension and the wedding that he had not got time to address this when it was raised. He had therefore asked his staff to keep an eye open and once he was satisfied that there was substance in the whisperings he confronted Mr Rahman one day in February. He told Mr Rahman that the staff had alleged that he had been stealing. He also, by way of bluff, told Mr Rahman (incorrectly) that a video camera had recorded him. Mr Rahman admitted stealing and when asked how he had done it, he said that when he collected cash from a customer who did not want change he would put the cash and the bill together in a passageway on the way into the kitchen and would later collect it whilst he was taking the plates through. Mr Khan apparently threatened to call the police but Mr Rahman started crying and knelt down and asked for forgiveness. He said he had not been doing it for very long and only when there was such a number of cash customers that no one would spot it. He told Mr Khan he came from a poor background and, seeing so much cash, he just could not resist it. Mr Khan agreed not to call the police but terminated his employment immediately.

61. Mr Khan told us that when he had named "Mr Rahman" as a trusted employee at the CIF interview, he was not referring to Shafiqur Rahman but to Syed Shahidur Rahman. He explained that being asked the question in 2007 he answered it as at that date.

62. Mr Khan, in his witness statement, stated that as far as real property is concerned his only asset was his equity in the matrimonial home. He also made reference to his increasing credit card debts. These had stood at between ten and twelve thousand pounds on 17th October 2007 and as at May 2013 had reached forty one thousand pounds.

63. In cross-examination, Mr Khan was asked about the various legal entities under which The Last Days of the Raj had traded and Mr Khan's involvement in each. He was very vague. When asked why the business of Tandoori, of which he had been a director and shareholder, had transferred to Cuisine, he could not recall. When asked if the goodwill in the business was transferred, he replied that HMRC should have that information. He was finally asked whether he was aware of the transfer to which he replied that it had been a long time ago.

64. In relation to the SCO enquiry, Mr Chapman's first question was to ask whether Mr Khan accepted that he had extracted income from the business. Mr Khan replied he did not. He had been forced to make admissions because he felt bullied, intimidated, threatened and scared to hell. He said he could not continue to deny suppression because he was so terrified of going to jail. He could not just walk away. He had believed that if he had tried to leave he would have been arrested and that they would only let him go when he had admitted to something. Mr Khan accused Mr

Ford of being "in the hands of HMRC". With regard to his admissions to the Hansard questions, Mr Khan was adamant that he only answered them in the affirmative at the end of the meeting and that when he had first been asked he had denied any wrongdoing. Mr Khan accepted that his answers to the Hansard questions constituted an admission of dishonesty but denied that he had been dishonest because he did not make the answers voluntarily. He described the officers' response to his denials. They called him a liar and told him to get out and think again and this happened time after time. Mr Chapman asked Mr Khan if he had understood that by signing the Disclosure Report he was admitting suppression. Mr Khan replied that he did not understand that. He had never read it. He had been crying and was upset and only signed the document so he would not go to prison. His children were young and his life was hell and he felt quite helpless. He just wanted to get on with his life and put it all behind him.

65. The tribunal then put the identical question to Mr Khan, namely did he know that he was admitting to omissions when he signed the document. This time Mr Khan replied "yes".

66. Mr Chapman next asked Mr Khan if he knew that by signing the documents he would be accepting adjustments of £120,000. To this Mr Khan replied "No I thought it was £90,000". (It should be noted that £34,000 had already been paid.). Mr Chapman then asked what he thought the £90,000 was for. He replied that he knew he would have to pay it but he did not know what for. He signed in order to start reliving his life so that they would stop chasing him and would go away. Mr Chapman finally put it to him that by signing the report he was accepting that he had acted dishonestly and in continuing to deny it, he was continuing to be dishonest. Mr Khan again denied any form of suppression and any dishonesty.

67. It should be recorded that during the above part of the cross-examination, Mr Khan became increasingly emotional and upset, threatening self-harm to the extent that the Tribunal saw the advocates alone and questioned whether medical attention should be sought for Mr Khan. Mr Nawaz appreciated the concern but took the view, as it turned out rightly, that Mr Khan could continue. We should also record here that Mr Chapman put these questions in an exemplary fashion. He stated in advance that they had to be put and he put them as gently as he could. He did everything he could to try and keep Mr Khan's distress to a minimum whilst setting out the case for the Commissioners.

68. Mr Khan was further asked by Mr Chapman exactly what he did once he had been alerted to the possibility of Mr Rahman stealing. He replied that he had told his staff to keep an eye open as he did not have the time to address the problem there and then and it might any way have only been a rumour. He knew he needed evidence or Mr Rahman could say that he had been unfairly dismissed. He did not approach Mr Rahman initially because he did not want to make a false accusation and be taken to the Employment Tribunal. He carried out a fact-finding exercise and then dismissed him when he had proper evidence. After the wedding was over more employees had come forward and had told Mr Khan that they had seen Mr Rahman stealing. They were all giving him similar information. Mr Khan accepted that he did not ask Mr

Rahman for how long he had been stealing or how much he had taken. He said that he could not press him because he was screaming and crying and was vulnerable.

69. Mr Khan, also in cross-examination, was asked to describe the cashing up procedure when he was not on duty. He described a manual till which did not operate on a till roll system. A £50 float was kept permanently in the till drawer.

70. At the end of each evening, one member of staff would add up the amount of the bills on a calculator and record the total on a plain slip of paper. The cash would then be added up and recorded on the same piece of paper and likewise the credit card slips. A note was also made of any expenditure. The bills, credit card slips and cash would then be bagged with the slip of paper recording the amounts, marked with the date and left out for Mr Khan. When Mr Khan was next in he would empty the bag, double check the amount, checking it tallied against the staff slip. He would then put the bills through his own adding machine. He kept the adding machine counterfoil as part of the business records and the total would be taken forward to the daily gross takings sheets which he completed weekly. At this point the staff slip would be destroyed. The kitchen chits would not be kept as they would be soggy and a health hazard. As far as tips were concerned, the staff were instructed to put these in a plastic bag in a small metal box, leaving a note at the end of each evening as to the amount. At the end of the week, Mr Khan would count the contents of the metal box. The total was recorded as takings. Round pounds were banked but smaller amounts were sometimes left in the box as the bank doesn't like them.

71. Apart from Mr Khan's oral and written evidence, Mr Nawaz put before us a statement which had been taken by Mr Khan and Mr Kellett on 21 January 2009 from a Mr Injat Ali. Mr Ali was one of the full time chefs and we believe him to have been "employee number 1" (paragraph 25 above) who had been interviewed by HMRC. Mr Ali described how he had been interviewed by six HMRC officers, three groups of two who interviewed him separately and consecutively. Mr Ali had never been shown or asked to check the accuracy of the HMRC statement which had been drawn up. He confirmed, inter alia, that Mr Khan would rarely come to the restaurant. He occasionally came on some lunchtimes and on Saturdays but for the remainder of the evenings, rarely. He confirmed that he had never seen Mr Khan destroy or burn restaurant meal bills. He confirmed that he had also told HMRC that whoever had been in charge of the restaurant in the evening would count the cash at closing time. He confirmed that he had been asked whether he knew anyone who had been sacked and he had replied yes "Pir" which was a nickname for Shafiqur Rahman. He also had told HMRC that he had not been paid any untaxed wages or untaxed tips or untaxed Christmas bonuses except for one £5 tip. He did not receive a share of the tips.

72. Mr Nawaz submitted a calculation designed to show the impact of the additional HMRC custom on the observation nights on the pattern of cash receipts. This calculation went through a number of revisions, the revision in final form before us being dated 12 January 2014. This purports to demonstrate that on the two observation days the amount of additional cash generated by the HMRC officers' meals represented a 74.43% increase in cash takings.

The validity of the VAT assessment

73. Mr Nawaz made two quite distinct challenges to the validity of the VAT assessment. The issue was raised briefly by Mr Nawaz in his oral submissions but was, with the agreement of both advocates, more fully argued by written submissions which were dated 2 April 2014 (Mr Nawaz,) 14 & 19 May (Mr Chapman) and 20 May (Mr Nawaz). We set out here as a preliminary issue both the arguments and our conclusions on these two points.

74. Mr Nawaz's first contention concerned the HMRC internal assessment form 645. Mr Nawaz had repeatedly requested disclosure of this form but, for no obvious reason and without any explanation, it had never been produced. Mr Nawaz's argument was that the failure to produce the form indicated that it did not exist and that without such a form the assessment could not have been properly issued. He drew the distinction which has long since been made by the courts between the issue and the notification of an assessment, arguing, in effect, both steps are essential to the process.

75. In response, Mr Chapman cited the definition of the VAT 645 which he had taken from the HMRC internal guidance manual. This defines the form as the "… input document which is used by the local office to notify the computer system of the acceptance and issue of an officer's assessment or error correction". The position of the Respondents, stated Mr Chapman, was that the Appellant had been deregistered for VAT by the time the VAT assessment was raised. As such the company was no longer on the computer system so the form could not be keyed into it. The adjustments were achieved manually by the issue of letters. Secondly, Mr Chapman asserted that the distinction between the issuing and notification of an assessment was relevant only to ascertaining the timing of the assessment. At the very latest, the making of an assessment is the date of notification and clearly there was a notification here and a valid one at that.

76. In his submissions on this point, Mr Nawaz had relied upon the tribunal decision in the case of *Courts PLC v Commissioners for Customs and Excise*. Mr Chapman cited the Court of Appeal decision in the same case (*Courts PLC v Customs and Excise Commissioners* [2005] STC 27), both of which we have read.

77. We reject Mr Nawaz's contention that the absence of a 645 invalidates the assessment. As Mr Chapman pointed out, and as clearly supported by the Court of Appeal in *Courts PLC*, there is no statutory process for making an assessment and the failure to follow internal procedures would not in any event invalidate the assessment. The critical point here has to be that the Appellant had been deregistered for VAT and the Commissioners were not therefore in any position to adopt a 645 procedure.

78. Mr Nawaz's second challenge to the validity of the assessment was its timing. An assessment has to be issued by the later of two dates, those dates being (i) one year from the Commissioners' coming into possession of facts sufficient to enable an assessment to be issued; and (ii) two years from the end of the period of assessment. Mr Nawaz contended that the last period for which the Commissioners had conceded that they had any evidence of wrongdoing was the period 01/05. The assessment

should therefore have stopped at 01/05 and the fact that it was issued on 16 December 2008 means that it was well out of time for the two year time limit for an assessment for a period ending 01/05 and considerably out of time also with regard to the one year time limit.

79. In response, Mr Chapman firstly referred to section 77(1) VAT Act 1974 which provided a long stop date after which an assessment could not be made of three years from the end of the prescribed accounting period. However in cases of dishonesty, as the Commissioners assert this case to be, the longstop date is extended to twenty years (section 77(4)).

80. Mr Chapman also submitted that in fact the assessment was raised within the prescribed periods in any event. The assessment raised on 16 December 2008 was made less than one year from HMRC coming into possession of facts sufficient to enable them to raise the assessment. He cited the judgment of Dyson J at paragraphs101-102 *Pegasus Birds Ltd v Customs and Excise Commissioners* [1999] STC 95.

> "1. The commissioners' opinion referred to in s73(6)(b) is an opinion as to whether they have evidence of facts sufficient to justify making the assessment. Evidence is the means by which the facts are proved.
>
> 2. The evidence in question must be sufficient to justify the making of the assessment in question (see *Customs and Excise Commissioners v Post Office* [1995] STC 749 at 754 per Potts J).
>
> 3. The knowledge referred to in s73(6)(b) is actual, and not constructive knowledge (see *Customs and Excise Commissioners v Post Office* [1995] STC 749 at 755). In this context, I understand constructive knowledge to mean knowledge of evidence which the commissioners do not in fact have, but which they could and would have if they had taken the necessary steps to acquire it.
>
> 4. The correct approach for a tribunal to adopt is (i) to decide what were the facts which, in the opinion of the officer making the assessment on behalf of the commissioners, justified the making of the assessment and (ii) to determine when the last piece of evidence of these facts of sufficient weight to justify making the assessment was communicated to the commissioners. The period for one year runs from the date in (ii) (see *Heyfordian Travel Ltd v Customs and Excise Commissioners* [1995] V&DR 1 at 10).
>
> 5. An officer's decision that the evidence of which he has knowledge is insufficient to justify making an assessment, and accordingly, his failure to make an earlier assessment, can only be challenged on *Wednesbury* principles,

or principles analogous to *Wednesbury* (see *Associated Provisional Picture Houses Ltd v Wednesbury Corp* [1948] 1 KB 223) (see *Classicmoor Ltd v Customs and Excise Commissioners* [1995] V&DR 1 at 10-11, and more generally *John Dee Ltd v Customs and Excise Commissioners* [1995] STC 941 at 952 per Neill LJ).

6. The burden is on the taxpayer to show that the assessment was made outside the time limit specified in s73(6)(b) of the 1994 Act."

81. Mr Chapman also referred us to *ERF Ltd v Revenue & Customs Commissioners* [2012] UKUT 105 (TCC) Mann J at paragraph 39 stated:

39. We think an overall view of the material does not yield a conclusion that the Tribunal reached the wrong view about Mr Harold's state of mind at the date of the meeting. Mr Harold formed his views in the run up to a meeting at which the new Approach was to be tendered. It is inherent in that approach that the taxpayer has an opportunity to present a factual case to HMRC, and HMRC holds off whatever it might do until the taxpayer has availed himself (or, we suppose, failed to avail himself) of it. In that context, it is a fair reading of the evidence that Mr Harold had been moving to an opinion which, if he were left entirely to his own devices, might well have crystallised to an opinion of dishonesty sufficient to amount to a piece of the jigsaw. But to have got to a state of finality about that in these circumstances would have gainsaid the purpose of the New Approach which was proffered bona fide to ERF. The relevant opinion of Mr Harold was that which he expressed towards the end of the meeting, which was that the matter would be approached with an open mind. It would have been disingenuous of him to have said that and in fact have had a firm, and irremovable opinion of dishonesty, and no one has suggested he was disingenuous. He was, in effect, invited not to have that opinion and he implicitly agreed. If one wants to pursue the metaphor, he might have been toying with the piece of jigsaw in his hand, but he was invited not to put it down lest it be the wrong piece, and he agreed with that. There is nothing *Wednesbury* unreasonable with that. This is essentially what the Tribunal found in paragraph 122 of its decision. This was not only a view which it was entitled to reach; it was in our opinion the correct view. "

82. It was Mr Chapman's contention, that the burden of proof being upon the Appellant, the Appellant had failed to establish that Mr Hancox was *Wednesbury* unreasonable in failing to make the assessment prior to 16 December 2008. He pointed out that Mr Nawaz had never put it to Mr Hancox in cross-examination that he was in fact in a position to make the assessment at an earlier date than that which he did.

83. Again we have to accept here Mr Chapman's contentions and reject Mr Nawaz's case that the assessment was raised out of time. For the very reasons put forward by Mr Chapman, it is clear that Mr Hancox was gathering evidence right the way up until he decided he had sufficient to raise the assessment. Meetings took place on 17 October 2007 and 17 June 2008 and representations were being made by Mr Khan's representatives as late as a letter dated 12 December 2008. Based on *ERF Ltd* the Respondents' investigations have to include a consideration of the Appellant's position and Mr Hancox throughout showed a willingness to listen and look at anything further that was put to him.

84. In summary therefore we reject both of the contentions of Mr Nawaz, namely that first the assessment was invalidly raised and secondly that it was out of time.

Submissions on behalf of the Commissioners

85. It was Mr Chapman's primary submission, that both in the non-declaration of the HMRC meals and in the observations, there was clear evidence of suppression. Whilst noting Mr Nawaz's challenges to the accuracy of the observations, he contended that there was no clear evidence that the observations were inaccurate and nothing to suggest that the officers had been unable to see who was in the restaurant, for example by walking round. No alternative to the number of observed diners had been put forward by Mr Khan. It was also Mr Chapman's contention that Mr Khan was present on the premises, at least during Mr Tait's shift. Mr Khan had submitted that with the exception of the pre-ordered meal on 9 December, none of the meal orders on either day were in his handwriting but Mr Chapman challenged this, opining that the handwriting on all orders was rather similar to Mr Khan's.

86. Mr Chapman submitted that Mr Khan was not a straightforward witness, his evidence being unfocussed, at times aggressive and on a number of occasions evasive. Of particular relevance was the SCO enquiry. The outcome of the enquiry was that Mr Khan had, by his own admission, been dishonest and yet his continued refusal before this tribunal to accept that damaged his credibility as a witness. Further his evidence in relation to the enquiry, and in particular the interview, was not credible given that he had been represented by two firms of accountants and it was they who had drawn up the Disclosure Report. It was not credible that Mr Khan would have signed the Disclosure Report, leading to a payment of £119,000 if in fact he had done nothing wrong. In that event, in any case, to have signed the report would itself have been dishonest. It was equally not credible that Mr Khan should have become aware of a whispering campaign about Mr Rahman's thieving in December but not only did nothing about it until February, but also continued to allow Mr Rahman to cash up and act as a manager. If Mr Khan's explanation as to the missing takings is disbelieved, the only logical explanation was that Mr Khan was himself responsible.

87. Mr Chapman contended that the assessments were, on the evidence available, raised to best judgment. Mr Hancox had calculated on the basis of Mr Tait's schedules that only 61% of the true cash sales had been recorded. There was a similar rate of suppression on both days and the rate was broadly similar to that declared in

the SCO enquiry. Further Mr Hancox had been entitled to rely upon the presumption of continuity.

Submissions on behalf of the Appellant

88. The case for Mr Khan was that he had not been involved in any defalcations and did not benefit in any way, as evidenced by the Commissioners' concession that they had not a shred of evidence to suggest assets or living expenditure which would have exceeded his known means. Nothing in the tip off letter had been found to be accurate and there was no evidence of suppressed purchases or off record wages.

89. Mr Nawaz was strongly critical of the observations, describing them as "the worst he had ever seen". The officers had not been properly briefed. The scoping plan was inaccurate and in fact had not been given to all the officers. Some officers had described themselves as sitting on tables for four which, on the plan, were marked as tables for two. Of those who did have the plan, none of them had followed the standard practice of marking where they had sat and marking the position of observed parties. Had they done so the accepted duplication on 9 December could not have taken place. Mr Nawaz suggested that the parties of three and eight would have stood out and thus that duplication was obvious. There may well have been further duplications of parties of two which would not have been obvious. The presence of the trellis would have obscured the view of a number of officers who could not have seen what they purported to have seen and in fact how good was their memory so many years after the event, bearing in mind that their witness statements were not taken until 2011? Mr Khan was not on the premises either day and the attempts to identify him were wrong. There were no meal bills in his handwriting and he was at that time fully occupied with hospital appointments, his extension and his daughter's wedding.

90. In fact, submitted Mr Nawaz, the non-HMRC parties on each of the two days were easily explained. On 27 November there were two parties who had pre-paid a deposit and on 10 December there were four such parties. It was the "invariable" practice that orders were taken and deposits paid the day before the meal took place. The 27 November parties would have therefore come in on the 26th and the 10 December parties on the 9th. The "suppressed" parties were therefore not paying customers on the observation days. That fits the four missing parties on 9 December and although this theory would lead to there being two suppressed parties on 26 November, it was Mr Nawaz's suggestion that HMRC had overlooked one of them.

91. Mr Khan had from the start raised the possibility of staff theft, even before he had known of the dates of the observations. He would not have known that both dates fell within the period of Mr Rahman's employment and further that the wages record would show that Mr Rahman had been working on both those days.

92. With regard to the SCO enquiry, Mr Nawaz repeated much of Mr Khan's evidence, stressing that neither Mr Ford nor Mr Hossain were experienced in such enquiries. The Disclosure Report suggested no wrongdoing in terms of underdeclaration of earnings as measured by concealed assets or income. Proposed

additions had been without basis or foundation and were arbitrary. Mr Khan accepted suppression only because he was feeling menaced and bullied. He was terrified, believing he faced years in jail if he did not own up to suppression. He had been totally innocent of any defalcations and had in fact not been aware of the allegations against him. It was plain, argued Mr Nawaz, that the SCO settlement had been wholly excessive. There was no way that an income approaching £432,510 less any allocations to wages or nominal allocations to cost of sales could ever be justified. An admitted legacy of £18,000 in one year had been used to infer additional takings of £18,000 in all years. Further, to use that false figure as a basis now to assess to further suppression was adding insult to injury and again without basis in either fact or law.

93. The assessment process did not bear scrutiny, submitted Mr Nawaz. Mr Hancox stated that he thought Mr Khan would have needed to abstract cash from his current company to pay the SCO settlement whereas in fact that settlement had been repaid by Mrs Khan. Mr Hancox had originally stated that he had relied on two main factors, the observations and the SCO admission. In fact he later admitted to a third factor – the possibility of property acquired in third party names. This was totally without foundation. There was nothing in the lifestyle of Mr Khan that could have given any support to the alleged suppression. At the time of the SCO enquiry, Mr Khan had been driving a BMW. Now he was driving a clapped out Nissan. His lifestyle was frugal. Further there was no justification in the extrapolation of the omitted takings forwards and backwards. Mr Nawaz attacked the presumption of continuity relying on *William Chapman v Commissioners for HMRC TC01593*. Mr Hancox had made no attempt to draw up a means or capital statement. Had he studied the SCO Disclosure Report he would have found a starting point for such a statement. Mr Khan kept good business records and certainly was not in breach of any statutory or legislative requirement in his record keeping. All meal bills were kept. A fully operational cashbook and bank records were kept. Wages records were maintained and when Mr Khan drew any surplus cash it was duly recorded in the cashbook and accounted for through the PAYE system.

94. It was Mr Nawaz's contention that the Commissioners had been responsible for such delay in this case that Mr Khan had been denied a right to a fair trial. He was particularly critical of the failure to even mention the observations and then the failure to give details despite being persistently asked to do so. This, argued Mr Nawaz, was totally contrary to the concept of openness in proceedings.

Consideration

95. It was common ground that the burden of proof is on Kells and Mr Khan in respect of the assessments but upon HMRC in respect of the dishonesty penalty. The standard of proof is the balance of probability.

96. It is not in dispute that to some extent, the Appellant has suppressed its takings. At the very least, the officers' meals were not recorded. The extent of the suppression depends upon our findings on the evidence before us. Equally it is not in dispute that the suppression has to have come about through the dishonest actions of an individual. It is not suggested that the failure to record certain meal bills was accidental or even

negligent. The Commissioners allege it was Mr Khan who was responsible for the suppression. Mr Khan alleges it was his employee Mr Shafiqur Rahman. Upon our findings on this point, a lot depends – not only the attribution of the penalty but the extent of the suppression. If we were to accept Mr Khan's evidence, the suppression would be limited in time to the period of Mr Rahman's employment. If we were to find Mr Khan to have been culpable then there would not be, of necessity, any such limit on the duration of the suppression.

97. We therefore begin with a consideration of the evidence and our findings as to who precisely was responsible for concealing the takings. For the reasons which we set out below, it is our considered view that we cannot accept Mr Khan's evidence and we find that it is he who was responsible for the suppression. There is just too much in Mr Khan's evidence that we find not to be credible for us to accept, without more, his assertion that it was Mr Rahman who was responsible.

98. There is a lot in Mr Khan's evidence which we find to have been unconvincing but in assessing his evidence, we take note of Mr Nawaz's cautionary words about Mr Khan's state of health. That Mr Khan has and has had significant medical problems is not in dispute. This is borne about by evidence put before us in the form of medical reports. We were given no expert medical view however which could lead us to assess the current difficulties which Mr Khan may have in understanding questions, how to word his answers and how well he is able to remember. Some of his answers were so vague and confused that no reliability could be placed upon them. We take for example his inability to explain the various incarnations of the trading entities, entities in which he was intimately involved. It is possible that Mr Khan was being deliberately evasive and obstructive but it is also possible that he really could not remember. The unfocussed nature of his replies gives some credence to it being a medical issue and on this we will give him the benefit of the doubt.

99. However there were other aspects of Mr Khan's evidence which were not in the least vague. His answers were emphatic, clear and quite unambiguous but lacked credibility. We find certain aspects of Mr Khan's evidence with regard to the SCO enquiry to be quite simply not credible. It was clearly an upsetting experience for Mr Khan and we fully accept he would have found the interview tough and traumatic. Mr Khan was adamant that he had suppressed no takings whatsoever and yet he signed up to a suppression of £119,000. – all this whilst being fully advised by two professionally qualified representatives. Why should they persuade him to admit to a suppression he totally denied? Equally we do not believe that in signing the disclosure, Mr Khan did not realise what he was signing. Mr Khan told us quite clearly that he did not understand that in signing the disclosure he was admitting to suppression. And yet his reason for signing was, he told us, so he would not go to prison. What did he think was in the document? What did he think that he was signing? What was he going to prison for? Even more difficult to believe is the assertion that until he saw the Settlement Report during the course of the current hearing, he had never known of the observations and "test eats" which had been carried out and which had formed the basis of the SCO enquiry. That there could be a seven hour interview during which these observations were never mentioned is in

itself not credible. Even more difficult to believe is that the two professional advisers were never told of the observations or that if they were told they never told Mr Khan.

100. We cannot accept as truthful either, Mr Khan's evidence as to his conduct of the theft enquiry. It is not credible that an astute businessman, as we believe Mr Khan to be, would be told of the theft by a named employee in November/December and do nothing about it until February, however many other matters he had on his mind. In his evidence in chief, Mr Khan merely blamed his other priorities – the wedding and the extension. In cross-examination, he gave a different reason altogether. He was worried about a possible employment tribunal case. He had to find the facts and he needed concrete evidence before he could take any action against Mr Rahman. Mr Khan went on to describe this period of December to February as a fact finding period and that once he then had proper evidence, he challenged Mr Rahman. The problem is that we had before us no evidence as to what had changed during this time. His explanation that he had asked his staff to keep an eye on Mr Rahman and then in February they came back to him and confirmed what had previously been only a rumour does not strike us as being the hard evidence which he believed he needed. The interview with Mr Rahman is itself equally unbelievable. He never asked him how much he had taken or over what period – both of which factors are vital for Mr Khan to assess the impact on his business. This was Mr Khan's business and it was his money which had been stolen and he never took any steps to find out how much

101. Mr Nawaz contended that Mr Khan could not have been personally responsible for suppressing the takings because he was not personally there. A great deal of the observation evidence which we heard centred on whether or not Mr Khan had been correctly identified as being on the premises. A number of the officers contended that he had been. Mr Khan was adamant that he had not. However, in fact, in the context of whether or not Mr Khan was responsible for the suppression of meal bills, it is immaterial whether he was there or not. This is because of the cashing up procedure which he had adopted. . The business records were not written up by Mr Khan until, at the very earliest, the day following the meals and collection of cash from the customers. There is no unbroken audit trail from the moment a customer pays his bill to the recording of the takings in the business records. The trail is broken when Mr Khan destroys the slip upon which the cashing up staff had recorded the amount which they had taken. There is no way of verifying whether or not the amount recorded by Mr Khan in the business records was the same figure as was recorded by the staff when they cashed up. To suppress a meal bill, Mr Khan would not have needed to have been on the premises. He could have just as easily done it when he was entering up his records. The trail would have been complete had he kept either the original bills or the kitchen copies, or a till roll and/or the cashing up slips. He kept none of them.

102. We accept that Mr Khan raised the possibility of staff thefts at the early stage in the enquiry and we also accept that he probably named Mr Rahman even before he knew the dates of the observations. However merely to make the assertion is not evidence. We have the evidence of the dates of Mr Rahman's employment and we also have before us the daily gross takings from 1 February 2004 to 30 January 2005. If Mr Rahman had been extracting cash, we would have expected that to be reflected

in a reduction in takings during the period of his employment. However we could find no such reduction reflected in the takings. We looked at the figures in a number of ways, carrying out a number of calculations but the link was just not there. Indeed in answer to questions from the Tribunal, Mr Khan accepted that there was no variation in the takings following Mr Rahman's dismissal. The takings, he said, remained "normal".

103. We do not believe that the staff interviews take matters any further. The interviews have not been put into statement form and are not therefore signed by the employees. They are merely headed "notes of meeting …." There is no record of the questions which were asked, only a summary of what the employee apparently said. We are not satisfied from these notes that the employee necessarily understood what he was being asked or that the officers necessarily understood what they were being told or correctly recorded what was being said.

104. We find equally unsatisfactory, but for different reasons, the statement which Mr Nawaz put in of the interview with Mr Injat Ali. The problem with this statement is that it was Mr Ali whom we have referred to as Employee No. 1 in the HMRC staff interviews. The answers he gave in the two interviews conflict. Mr Ali had told the Respondents that Mr Khan was "always there". He had told Mr Kellett that Mr Khan rarely came to the restaurant. He told the Respondents that one employee, whose name he could not recall, had been dismissed in 2002 or 2003. When interviewed by Mr Kellett, he said that he had told HMRC that it was Pir who had been sacked. There may be many reasons for the discrepancies between the statements. Not least, it may be that Mr Ali, answering in the presence of Mr Khan, gave answers which he believed Mr Khan wanted him to give. This however is not a finding which we can make as we did not hear oral evidence from Mr Ali and we can do no better than disregard the statements completely.

105. Having concluded and finding as a fact that it was Mr Khan who was responsible for the suppression, we now look at the assessment itself. Mr Hancox had before him clear evidence of suppression derived from the observations. Mr Nawaz was highly critical of the way the observations had been carried out but his contentions with regard to them were somewhat contradictory. He first submitted that the observations were so flawed that their accuracy had to be in doubt. However he then went on to justify the non recording of the non-HMRC bills by attributing the presence of the precise number of parties to their having come in to pay their deposits for the following day. We accept that it would be common practice for a deposit to be requested and paid by larger parties. We accept that this deposit would obviously be paid sometime in advance of the meal but the suggestion that the deposit would "invariably" be paid the day before, as put to us by Mr Nawaz, is just not realistic. It is unfortunate that Mr Nawaz did not put this suggestion to the observation officers when they were giving their evidence. When the officers gave their evidence, all that was before the tribunal in this respect was Mr Khan's written witness statement when, in paragraph 28, he merely refers to people coming in "prior to their party bookings" to pay their deposits. It was not until he gave his oral evidence very much later that it was contended that deposits were always taken the previous day. The officers were given no opportunity to comment and we cannot accept this bald assertion which was

never able to be tested. We reject the suggestion that the non recording of the non-HMRC bills could be explained by people paying their deposits. The observation process may not have been perfect but there is no evidence it resulted in any undetected mis-recording. There was one duplication which was picked up but no evidence of any other. We accept the amended findings of the observations. The observations told Mr Hancox that almost every cash bill was not finding its way into the records.

106. Mr Hancox had himself not accepted Mr Khan's attempt to lay the blame on Mr Rahman and there was therefore no reason for him to limit the duration of the suppression. Given our findings on this as well, we find that Mr Hancox was fully entitled to raise an assessment and to extrapolate it backwards and forwards.

107. We have greater difficulty when we come to look at the quantum of the assessment and to consider whether or not it was raised to best judgement. Looking first at the methodology adopted by Mr Hancox, this is, in our view, quite seriously flawed and has resulted in an assessment that we find to be significantly excessive. Mr Chapman referred to Mr Hancox's approach as "broad brush" which doesn't exactly give one confidence in it. We have quite specific objections to the methodology. First it is based entirely on the omitted HMRC meals. This is custom which was parachuted into the restaurant. It is not custom that would be repeated and gave the restaurant a completely unrepresentative amount of cash sales for those two days. No adjustment is made for fluctuations in trade. What Mr Hancox had done is to calculate a daily suppression rate and use it for every single day of the year for a number of years. There is no adjustment for days of the week and no seasonal adjustments. In calculating omitted profits for corporation tax he does not reduce the sales by the VAT element and makes no cost of sales deduction.

108. We are also exercised by the refusal of the Respondents to disclose the observation dates. Mr Hancox was unable to give any good reason why this was not done. He was repeatedly asked for the dates but refused to give them until he had raised the assessment, following which, without any evidence that anything had changed, he provided them. This conduct was deplorable and we very much hope that it no longer represents HMRC practice. However it has to be said that Mr Khan gave no evidence that he was prejudiced by the delay in providing the dates. There was no suggestion that he could or would have been able to better present his case had he had knowledge of the dates. Looked at in the context of whether Mr Hancox was deliberately preventing Mr Khan from making his case, there is no evidence that Mr Khan could or would have provided any further material that would have made any difference either to the decision to assess or the amount of the assessment.

109. Mr Hancox was also demonstrably under certain misapprehensions when he raised his assessment. He believed, in our view quite wrongly, that this was an "upmarket" establishment with a prestigious clientele. He also believed he had hard evidence of Mr Khan having an interest in a property in another's name. This concerns us for two reasons. First it turned out, in relation to that property at least, to be just wrong. Secondly it was not disclosed to the tribunal until the closing moments of Mr Hancox's evidence and then came out almost by accident. Mr Hancox

admitted that this was a factor which he had taken into account in his decision to assess and yet it was not referred to in his witness statement or his evidence in chief.

110. All these factors we have weighed up in our consideration of whether or not the assessment was raised to best judgment.

Best Judgment

111. We set out here what we take from the leading cases to which we were taken by the parties. In *Van Boeckel v Customs and Excise Commissioners* 1981 STC 290. Woolf J (as he then was) stated therein as follows:

> "Therefore it is important to come to a conclusion as to what the obligations placed on the Commissioners in order properly to come to a view as to the amount of tax due, to the best of their judgment. As to this, the very use of the word 'judgment' makes it clear that the Commissioners are required to exercise their powers in such a way that they make a value judgment on the material which is before them. Clearly they must perform that function honestly and bona fide. It would be a misuse of that power if the Commissioners were to decide on a figure which they knew was, or thought was, in excess of the amount which could possibly be payable, and then to leave it to the taxpayer to seek, on appeal, to reduce the assessment.
>
> Secondly, clearly there must be some material before the Commissioners on which they can base their judgment. If there is no material at all it would be impossible to form a judgment at to what tax is due.
>
> Thirdly, it should be recognised, particularly bearing in mind the primary obligation, to which I have made reference, of the taxpayer to make a return himself, that the Commissioners should not be required to do the work of the taxpayer in order to form a conclusion as to the amount of tax which, to the best of their judgment, is due. In the very nature of things frequently the relevant information will be readily available to the taxpayer, but it will be very difficult for the Commissioners to obtain that information without carrying out exhaustive investigations. In my view, the use of the words 'best of their judgment' does not envisage the burden being placed on the Commissioners of carrying out exhaustive investigations. What the words 'best of their judgment' envisage, in my view, is that the Commissioners will fairly consider all material placed before them and, on that material, come to a decision which is one which is reasonable and not arbitrary as to the amount of tax which is due. As long as there is some material on which the Commissioners can reasonably act then they are not required to carry out investigations which may or may not result in further material being placed before them."

112. We were referred by both parties to the following cases:

Rahman (trading as Kayam Restaurant)(No.1) v CEC [1998] STC 826 ("*Rahman No 1*")

Rahman (trading as Kayam Restaurant)(No2) [2003] STC 150 ("*Rahman No 2*")

Pegasus Birds v HMRC [2004] EWCA Civ 1015

113. In *Rahman No 1*, commenting on Woolf J's judgment in *Van Boeckel*, Carnwath J (as he then was) stated as follows:

> "I have referred to the judgment in some detail, because there are dangers in taking Woolf J's analysis of the concept of 'best judgment' out of context. The passages I have italicised show that the tribunal should not treat an assessment as invalid merely because it disagrees as to how the judgment should have been exercised. A much stronger finding is required; for example, that the assessment has been reached 'dishonestly or vindictively or capriciously'; or is a 'spurious estimate or guess in which all elements of judgment are missing'; or is 'wholly unreasonable'. In substance those tests are indistinguishable from the familiar *Wednesbury* principles (See *Associated Provincial Picture Houses ltd v Wednesbury Corp* [1948 1 KB 223). Short of such a finding, there is no justification for setting aside the assessment.

114. In *Rahman No 2*, Chadwick LJ stated at paragraph 32:

> "In such cases … the relevant question is whether the mistake is consistent with an honest and genuine attempt to make a reasoned assessment of the VAT payable; or if it is of such a nature that it compels the conclusion that no officer seeking to exercise best judgment could have made it. Or there may be no explanation; in which case the proper inference may be that the assessment was indeed arbitrary".

115. In *Pegasus Birds*, Carnwath LJ stated:

> "The Tribunal should remember that its primary task is to find the correct amount of tax, so far as possible on the material properly available to it, the burden resting on the taxpayer. In all but very exceptional cases, that should be the focus of the hearing, and the Tribunal should not allow it to be diverted into an attack on the Commissioners' exercise of judgment at the time of the assessment."

Consideration of best judgment

116. This assessment comes perilously close to not having been raised to best judgment but we are mindful of the tests laid down in the cases to which we have referred. In no way can it be said that Mr Hancox acted dishonestly or vindictively or capriciously. The assessment which he raised was not "a spurious estimate or guess in which all elements of judgment are missing". Most importantly, having made his calculation, he had a point of cross-reference. He knew that in the SCO enquiry, Mr Khan had admitted to suppression of £1600 per week which was close to the figure that Mr Hancox had just reached himself. We have heard a great deal of evidence as

to the accuracy or otherwise of the SCO findings but the relevance here is that Mr Hancox was fully entitled to rely upon the signed declaration of suppression.

117. Given the very high threshold which has to be reached before an assessment can be said not to have been raised to best judgment, we find that this assessment was raised to best judgment and following from that finding and from the cases to which we have referred, we accept it as our role and our "primary task" to find the correct amount of tax due. This approach falls in with that agreed by the parties, namely that if we were satisfied that the assessment had been raised to best judgment we were then entitled to look afresh at the figures and reach our own view of what the correct amount of tax should be.

Our calculation of the tax due.

118. In the methodology which we have adopted, we seek to remove a number of the flaws which we identified in Mr Hancox's calculation. Our calculation of the rate of suppression does not rely on the HMRC bills. It also factors in the cost of sales and takes account of seasonal variation and price changes. In reaching our calculation, we have looked only at the two observation days as those are the only two days for which we have a sufficiently full set of figures. We have acted on the premise that the value of a meal bill is not dictated by or reflected in the method of payment. We have ignored takeaways as the parties had both done despite evidence that cash takeaways had gone unrecorded. We are also mindful of the fact that the observations took place in the run up to Christmas when there would be much more likelihood of larger parties which would not be representative of the rest of the year.

119. On 26 November 2004, taking out the HMRC bills none of which were declared, there were eleven recorded dining parties (page 274 hearing bundle). The total of those bills came to £534.90 giving an average dining bill of £48.63. There were no large parties, and even though the one bill for £125.95 might give the impression of so being, we note that there were only 4 main courses. There was one non HMRC unrecorded cash bill. Taking £48.63 as the value of the unrecorded third party cash sale, we calculate this as representing 5.56% of the declared sales for that night.

120. On 9 December (page 281 hearing bundle), there were two large parties, the bills for both of which we have left out of account as being unrepresentative and there were two recorded HMRC parties which we have also left out of account. There were nine other dining parties. We calculate the average dining bill of these nine parties to be £58.19. Taking this as the value of each unrecorded third party cash sale, the four non HMRC unrecorded sales represent 22.93% of total declared sales less the two HMRC declared bills.

121. We have averaged the suppression percentages for each of these two evenings at 14.24%. This therefore is our calculation of the daily rate of suppression. Applying this to the total recorded turnover for the year of £370,441.74, we reach unrecorded sales of £52,769.34. This figure is inclusive of VAT which should be taken into account. As agreed with the parties we have done the calculation for 2004/05 leaving

the parties to adopt our method of calculation and rate of suppression for remaining years. For this year only, the unrecorded HMRC meals of £462.40 have to be added back in. This then gives a total unrecorded VAT inclusive turnover of £53,231.74 which, less VAT of £7,928.13, gives an additional turnover for the year of £45,303.61. We received no evidence of gross profit percentage and this should be obtained from the company's accounts and applied to this turnover figure to give the additional profits for the year. These profits, which are not recorded in Kells' books, are all to be treated as additional wages to Mr Khan, resulting in a recalculation of the Reg 80 assessments on Kells, and the income tax assessments on Mr Khan.

122. Given that, on our findings, it was Mr Khan who was responsible for the suppression, we see no reason why the presumption of continuity should not apply. Mr Nawaz argued that it should not, relying on *William Chapman*. The tribunal in *William Chapman* found sufficient changes in trading pattern to "negate any presumption of continuity which might otherwise have been justified". Fundamental to the current case is however the SCO enquiry which gives strong support to a continuing suppression. We believe there is full justification for taking this suppression back to 2002/3 and forward to 2007/8 and the methodology we have set out above should be applied to the accounts for those years to give the figures for omitted profits.

123. We appreciate, as Mr Nawaz pointed out, that there is no evidence of where the suppressed takings went. We accept that there is no evidence of expensive lifestyle and there is not evidence before us of hidden assets but the mere fact that we don't know where there money went cannot provide justification for finding that there was no such suppression when there are a sufficient number of other factors to persuade us that there was a suppression of this approximate amount and it was Mr Khan who was responsible. We believe that benchmark is met here.

124. We have considered Mr Nawaz's contention that the delays and lack of earlier or complete discovery resulted in the denial of a right to a fair hearing. We have touched on this earlier in this decision when considering the effect of the failure to disclose observation dates. There is no evidence before us that Mr Khan has been denied a fair trial and he did not seek to argue that he had been in any way prejudiced by any delay which there had been. This contention is therefore rejected.

Penalties

125. Mr Hancox having concluded that there had been suppression and that that suppression had been dishonest, on 16 December 2008 raised a civil penalty pursuant to section 60 VAT Act 1994. Having further concluded that the dishonesty was down to Mr Khan, he also, again by letter dated 16 December 2008, assigned the penalty to Mr Khan pursuant to section 61. In issuing the penalty, Mr Hancox allowed mitigation of 35%. We were referred in evidence to Mr Hancox's Penalty Submission dated 5 November 2008 in which he set out his reasoning both for attributing the penalty to Mr Khan and for arriving at the amount of mitigation. In relation to the attribution, he submitted to his authorising officer that it would be difficult to accept that a businessman of Mr Khan's experience would have so little

cash control that his employees could extract such large amounts from the restaurant without his appreciating it. He concluded that "the reality of the situation seems to be that he has simply continued the practices that were in place at the time of the SCO enquiry". In relation to mitigation, he recommended no mitigation under the heading "Early and truthful explanation" in that he believed that there never had been any full and truthful explanation. In response to the "fully embracing and meeting responsibilities" factor, he pointed out that Mr Khan had attended the open meeting and answered the questions put to him. He did not believe that Mr Khan had answered the questions honestly but confirmed that he had provided all documents and information requested. He therefore recommended mitigation of 35%. His authorising officer, Mr M J Howlett, agreed to the issue of the 65% penalty.

126. Before us it was Mr Nawaz's case that Mr Khan had not been dishonest and had not been responsible for the thefts. His case therefore was that there should have been no attribution of the penalty to Mr Khan. He did not specifically address us on quantum or the degree of mitigation allowed.

127. For the reasons already given in this decision, we have concluded that Mr Khan did act dishonestly and was responsible for the suppression. We therefore fully accept that the Commissioners were entitled to assign the dishonesty penalty to Mr Khan. As far as mitigation is concerned, we believe Mr Hancox acted quite fairly. He accepted in cross-examination that Mr Khan had been fully co-operative and had provided whatever information and documents were sought. We therefore uphold the attribution of the penalty to Mr Khan and we uphold the degree of mitigation given. The amount will of course now vary pursuant to our alternative calculation of the suppression.

Summary of our conclusions

128. For all the reasons given above, the appeal is allowed in part. We find as a fact that Kells, through its director Mr Khan, dishonestly suppressed its takings. We also find as a fact that the Commissioners were fully justified in raising assessments and determinations to make good the loss of tax. We find that the assessment to VAT was validly raised and was raised to best judgement, but the amount of suppression used by Mr Hancox was excessive. The assessments and determinations under appeal should therefore be recalculated as directed in this decision. We also uphold the imposition of the penalty for dishonesty and its attribution to Mr Khan. We uphold the degree of mitigation allowed by Mr Hancox but the final amount due will stand to be recalculated.

129. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to

"Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

LADY MITTING
TRIBUNAL JUDGE

RELEASE DATE: 4 June 2014